

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

In the matter of XO Illinois, Inc.)

Petition for Arbitration Pursuant to)

Section 252(b) of the Telecommunications)

Act of 1996 to Establish an Interconnection)

Agreement with Illinois Bell Telephone)

Company d/b/a Ameritech Illinois)

Docket No. 01-0466

ADDITIONAL TESTIMONY

OF

ERIC L. PANFIL

On Behalf of
AMERITECH ILLINOIS

August 17, 2001

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OFFICIAL FILE

I.C.C. DOCKET NO. 01-0466
Ameritech Exhibit No. 3

Witness

Date 8/21/01 Reporter AV

1 Q. ARE YOU THE SAME ERIC L. PANFIL WHO TESTIFIED PREVIOUSLY IN
2 THIS DOCKET?

3 A. Yes, I am.

4 Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?

5 A. The purpose of this testimony is to address Ameritech Illinois's position in response to
6 the Commission Staff's positions as expressed in the testimony of James Zolnierrek.

7 Q. WHAT ASPECT OF DR. ZOLNIEREK'S TESTIMONY WILL YOU ADDRESS
8 FIRST?

9 A. On pages 19-35 of his testimony, Dr. Zolnierrek engages in a lengthy discussion of the
10 proposal of Ameritech Illinois to use bifurcated rates (i.e. separate setup and duration
11 charges) rather than simple per-minute rates for the reciprocal compensation of 251(b)(5)
12 traffic in the agreement with XO Communications. He concludes that he cannot
13 currently support the adoption of bifurcated rates, based on certain issues he identifies,
14 but that Staff is open to supporting bifurcated rates if their concerns and questions are
15 addressed.

16 Q. DO YOU AGREE WITH HIS CHARACTERIZATION (PAGE 20) OF THE
17 BIFURCATED RATE PROPOSAL AS AN ATTEMPT TO "CIRCUMVENT"
18 THE FCC'S *ISP COMPENSATION REMAND ORDER*?

19 A. Absolutely not. The Company's desire to implement bifurcated rates is not dependent on
20 its decision regarding the imposition of rate caps on ISP-bound traffic. It is certainly
21 difficult to explicitly and clearly determine the extent to which other types of traffic are
22 also driving differences in average hold times among carriers' networks, given the large
23 amounts of ISP-bound traffic currently in the mix and the uncertainty over the
24 identification of that traffic. But we are convinced that the differences in effective prices
25 for traffic with different hold-time characteristics, and the potential for regulatory
26 arbitrage offered by simple per-minute rates (particularly in conjunction with legislative

1 mandates for residential flat-rate "local" calling), make it imperative to move to a rate
2 structure that more accurately reflects the nature of cost causation for transport and
3 termination of traffic, particularly since there is no significant cost to changing the rate
4 structure. We are committed to the goal of adopting a bifurcated rate structure regardless
5 of our ultimate decision regarding the implementation of the FCC rate caps for
6 ISP-bound traffic, and intend to file revisions to our current tariffed reciprocal
7 compensation rates, based on our most recent cost studies, in the near future.

8 **Q. ON PAGES 23-27, DR. ZOLNIEREK DISCUSSES THE NEED FOR A BETTER**
9 **UNDERSTANDING OF THE COSTS AND BENEFITS OF A CHANGE TO**
10 **BIFURCATED RATES. DO YOU BELIEVE THAT THE BENEFITS**
11 **OUTWEIGH THE COSTS?**

12 **A.** Yes. As I mentioned in my response to the previous question, there is no significant cost
13 to Ameritech Illinois in implementing bifurcated rates to replace the current simple
14 per-minute rates, nor do I believe that other carriers will be significantly impacted. The
15 message recordings that are currently used to bill the simple per-minute rates already
16 contain all of the information necessary for the billing of bifurcated rates, so no changes
17 to the network or the message recording equipment are needed. Ameritech's billing
18 systems are already being updated to handle bifurcated rates that are in effect in Michigan
19 and will presumably also be in place later this year in Wisconsin. In any case, those
20 billing system changes are quite simple and straightforward. Most other carriers will also
21 be updating their billing systems to accommodate bifurcated rates regardless of whether
22 such rates are adopted in Illinois (for example, XO also operates in Michigan), and in any
23 case the changes required are, as I stated earlier, not at all difficult to implement.

1 **Q. ON PAGE 23 OF HIS TESTIMONY, DR. ZOLNIEREK CITES TO HIS**
2 **INFERENCE THAT AMERITECH MAY HAVE IN THE PAST VIEWED**
3 **BIFURCATED RATES AS NOT BEING COST EFFECTIVE. IS THIS**
4 **INFERENCE ACCURATE?**

5 A. No. That inference assumes that there was some consideration given in the past to using
6 bifurcated rates and that the idea was rejected. I have been involved in the development
7 of interconnection and reciprocal compensation arrangements since before the federal
8 telecommunications act came into being, and in my experience that is not the case.
9 People merely assumed that simple per-minute rates (like the access rates that had been in
10 effect for many years) would be adequate, and there was never any consideration or
11 discussion that I am aware of as to whether such rates presented any potential for
12 regulatory arbitrage. It is only after actual experience in the real world that we have
13 come to recognize the potential problems (because they have become actual problems),
14 and to identify the rate structure modification that will provide some degree of relief.

15 **Q. ON PAGE 29, DR. ZOLNIEREK EXPRESSES CONCERN THAT ANY**
16 **FINANCIAL BENEFITS THAT ACCRUE TO AMERITECH ILLINOIS DUE TO**
17 **A CHANGE IN RECIPROCAL COMPENSATION RATES WILL BE**
18 **DETRIMENTAL TO COMPETITION AND TO ILLINOIS CONSUMERS. HOW**
19 **DO YOU RESPOND?**

20 A. I certainly agree that it is likely that the change in rate structure will, in the short run,
21 benefit Ameritech Illinois, but that is hardly a rational basis on which to judge the
22 desirability of the change. The rate proposal should stand or fall (or be modified) based
23 entirely on whether it produces rates that are accurately reflective of the cost
24 characteristics of the service provided. Economically efficient rates are desirable due to
25 the long term economic benefits that will result from the development of competitive
26 service providers that seek to benefit from the provision of innovative, and truly
27 cost-effective services to consumers, not from the proliferation of service providers

1 focused on profiting from the exploitation and perpetuation of economically irrational
2 regulatory arbitrage opportunities. If the business plan of XO or any other carrier is
3 dependent on the continued availability of regulatory arbitrage opportunities, which by
4 definition provide no long term economic or social benefits to the public, then that carrier
5 is providing neither real competition nor real benefits to Illinois consumers.

6 **Q. ON PAGES 31-34 DR. ZOLNIEREK DISCUSSES QUESTIONS AND CONCERNS**
7 **REGARDING THE TWO COST STUDIES PROVIDED TO STAFF BY**
8 **AMERITECH ILLINOIS IN RESPONSE TO DATA REQUESTS. WHAT IS**
9 **YOUR RESPONSE TO THESE QUESTIONS AND CONCERNS?**

10 **A.** First, in response to the concerns expressed regarding the differences between the two
11 Ameritech Illinois cost studies, I would make the following two points. The cost studies
12 were performed approximately four years apart, which is sufficient time for some of the
13 costs, particularly those that are specific to our rapidly evolving wholesale operations, to
14 have changed. Also, the fundamental methodology for performing the cost studies for
15 the switching and transport cost elements was entirely changed between the two studies,
16 and it is my understanding that one of the main factors driving the changes to the cost
17 methods were criticisms leveled against the previous cost studies by Staff and the
18 Commission in earlier proceedings.

19 In regard to comparisons between the Illinois costs (on the one hand) and the cost-
20 based rates in Michigan and Texas, I would point out that the Michigan rates are not
21 based on Ameritech Michigan cost studies, but on alternative studies submitted by
22 another party in the Michigan cost proceeding that were ultimately adopted by the
23 Michigan Public Service Commission, and that the Texas rates are based on relatively old
24 cost studies that I understand were based on cost methods entirely different than those
25 employed either now or in the past by Ameritech, as well as being reflective of an

entirely different structure of traffic measurement and billing (i.e. originating carrier measurement). I don't believe that either one represents an appropriate benchmark for assessing the reasonableness of the Ameritech Illinois cost studies.

Q. WOULD YOU PLEASE SUMMARIZE AMERITECH ILLINOIS'S POSITION ON THE ISSUE OF BIFURCATED RATES, GIVEN THE CONCERNS EXPRESSED BY STAFF?

A. Ameritech Illinois continues to believe that the introduction of bifurcated rates in this proceeding is appropriate, and that the benefits to the public and to the development of economically sound and beneficial competition far exceed any minor and transitory costs of implementation. We believe that these benefits will exist regardless of whether, or when, Ameritech Illinois chooses to adopt the rate caps for ISP-bound traffic specified in the FCC's *ISP Compensation Remand Order*. To the extent that there is any concern over the proper level of the bifurcated rates, Ameritech believes it can alleviate them by offering to allow XO to make certain choices as to the initial rates that would be applicable under this agreement. First, XO will be permitted to choose either of two sets of bifurcated rates to be applicable upon the initial implementation of its agreement: either the rates offered in the Amendment attached to Ameritech Illinois's Response to XO's petition for arbitration, or the rates that will be filed soon in Ameritech Illinois's tariff (to which I referred above). In either case, the rates would ultimately be conformed on a forward-going basis to the approved rates in Ameritech Illinois's tariff, once the tariff goes into effect. In addition, Ameritech Illinois will allow XO to choose, at the time the agreement is submitted for approval, whether (or not) the terms of the agreement will call for a retroactive true-up of the rates paid for the period of time between the initial effective date of the agreement and the date on which the rates in the agreement are conformed to the new rates in the Ameritech Illinois tariff.

1 Q. WHAT OTHER ASPECT OF DR. ZOLNIEREK'S TESTIMONY WOULD YOU
2 LIKE TO ADDRESS?

3 A. On pages 2-3 of his testimony, and later on pages 17-19, Dr. Zolnierек recommends that
4 the Commission require that Ameritech Illinois make an immediate decision to either
5 adopt the caps on intercarrier compensation rates for ISP-bound traffic specified in the
6 FCC's *ISP Compensation Remand Order*, or to forego the adoption of the caps. He also
7 appears to believe that if Ameritech Illinois chooses not to implement the rate caps at this
8 time, the Commission may forbid the Company from electing to implement the rate caps
9 at any future time. Ameritech Illinois does not believe that the Commission can lawfully
10 prevent the Company's adoption of interstate rates to be applied to interstate traffic under
11 the terms of an FCC order.

12 Q. IS AMERITECH ILLINOIS'S DECISION TO DEFER ITS DECISION AS TO
13 THE APPLICATION OF THE RATE CAPS A FORM OF "ANTICOMPETITIVE
14 BEHAVIOR" AS DR. ZOLNIEREK CLAIMS?

15 A. Absolutely not. The FCC very deliberately and explicitly left the decision as to when (or
16 whether) to declare its intention to implement the rate caps up to each ILEC on a state-
17 by-state basis. In structuring its order, the FCC understood that situations varied among
18 states and carriers as to factors such as the remaining life of preexisting agreements and
19 the existence of varying types of "change of law" provisions (including some that
20 specifically reference the FCC docket which resulted in the *ISP Compensation Remand*
21 *Order*). Under the circumstances, the FCC chose to structure its compensation plan in a
22 manner that provides a great deal of flexibility, but also uncertainty, for all of the carriers
23 (including Ameritech Illinois) to which it applies. It creates a complex range of
24 possibilities, in which each carrier must make its business decisions based on the full
25 range of options available to it. The ability of ILECs such as Ameritech Illinois to

1 choose whether and when to invoke the rate caps for ISP-bound traffic is certainly one
2 source of uncertainty, but it is far from the only one. Even if the Company should choose
3 to invoke the rate caps, there will be uncertainty as to which existing agreements will be
4 subject to change at which points in time, based on their varying "change of law"
5 provisions; uncertainty as to the effective date of the capped rates in each such
6 agreement; and uncertainty as to whether the FCC's default proxy for identification of
7 ISP-bound traffic will be determined to be adequate by both parties to each agreement.
8 Certainly, there are other sources of uncertainty also, such as the efforts by CLECs to
9 have the FCC's *ISP Compensation Remand Order* overturned in the courts. That is
10 apparently an uncertainty that the CLEC industry believes it can live with, though it
11 plainly raises the level of uncertainty for ILECs as well as CLECs in planning for the
12 future.

13 **Q. HAS AMERITECH ILLINOIS ELECTED TO AVAIL ITSELF OF THE RATE**
14 **CAPS SPECIFIED IN THE FCC ORDER?**

15 A. Not at this time, though of course Ameritech Illinois will continue to monitor and analyze
16 developments in Illinois and may determine that it would be prudent to do so at some
17 point in the future.

18 **Q. DOES THAT FACT MERIT THE IMPORTANCE THAT DR. ZOLNIEREK**
19 **SEEMS TO ASSIGN TO IT IN THIS ARBITRATION PROCEEDING?**

20 A. No. The *ISP Compensation Remand Order* does not condition its elimination of 252(i)
21 rights regarding intercarrier compensation for ISP-bound traffic on whether or not an
22 ILEC chooses to adopt the rate caps for that traffic. The Order establishes the FCC's
23 jurisdiction over ISP-bound traffic, and specifies the compensation to be applied to that
24 traffic under the terms of that Order, regardless of whether the ILEC chooses the option
25 of imposing the rate caps. So, regardless of whether the rate caps are imposed, the

1 compensation for ISP-bound traffic must take place under the auspices of the *ISP*
2 *Compensation Remand Order*, not pursuant to section 251(b)(5) of the Act, and must be
3 specified as such in the agreement for the compensation to occur. Ameritech Illinois
4 believes that the terms of compensation must be explicitly and completely spelled out in
5 the interconnection agreement.

6 Ideally, I believe the provisions of the agreement between XO and Ameritech
7 Illinois should fully reflect *all* aspects of the compensation plan set forth in the FCC's
8 *ISP Compensation Remand Order*, including terms and conditions related to the optional
9 rate caps, so that the agreement would not need to be amended in order to accommodate
10 the application of the rate caps on ISP-bound traffic, should Ameritech Illinois declare its
11 intent to impose the caps and satisfy the prerequisite established by the FCC. Given the
12 potential complexities of those provisions and the likely interest of other parties in the
13 same issues, that full task is not really amenable to this arbitration process, and
14 Ameritech Illinois has not sought to introduce all of those issues here. But the Company
15 does seek, as the end product of this proceeding, an agreement that clearly provides the
16 framework for full implementation of the FCC's compensation plan, in order to eliminate
17 the potential for unnecessary disputes in the future. Ameritech Illinois believes that the
18 Amendment that it has offered to XO accomplishes that reasonable goal.

19 **Q. DO YOU BELIEVE AN AGREEMENT THAT CONTAINS "RATES, TERMS,**
20 **AND CONDITIONS SIMILAR TO THOSE IN THE AMERITECH-FOCAL**
21 **ARBITRATED INTERCONNECTION AGREEMENT," AS RECOMMENDED**
22 **BY DR. ZOLNIEREK ON PAGE 4 OF HIS TESTIMONY, WOULD BE**
23 **CONSISTENT WITH THE REQUIREMENTS OF THE FCC?**

24 **A.** No. The agreement at minimum must explicitly acknowledge the FCC's jurisdiction over
25 that traffic, specify the compensation arrangements that will apply so long as Ameritech
26 Illinois does not adopt the FCC rate caps, and provide a foundation for the potential

1 implementation if the rate caps on ISP-bound traffic in the future. An agreement that
2 does all of these necessary things would not be "similar to" the Focal agreement, though
3 it could effectively result in the same rates being applied to 251(b)(5) traffic and
4 ISP-bound traffic for some period of time.

5 **Q. ON PAGES 10-13 OF HIS TESTIMONY AND ALSO ON PAGE 30,**
6 **DR. ZOLNIEREK INDICATES A CONCERN THAT UNDER AMERITECH**
7 **ILLINOIS'S PROPOSAL, PHYSICAL INTERCONNECTION BETWEEN**
8 **NETWORKS MAY NEED ALTERATION TO ACCOMMODATE THE**
9 **MEASUREMENT OF ISP-BOUND TRAFFIC. IN YOUR UNDERSTANDING,**
10 **DOES THE PROPOSAL ACTUALLY RAISE ANY SUCH CONCERNS?**

11 **A.** No, it does not. There is nothing in Ameritech Illinois's proposed amendment that is
12 intended to require the alteration of physical interconnection or trunking arrangements. I
13 do not believe it is necessary to alter the interconnections in order to directly identify
14 ISP-bound traffic in a reasonable manner. ISP-bound traffic can be identified using data
15 produced by existing traffic measurement and recording capabilities, combined with
16 reasonable efforts to identify and track the telephone numbers that are used for dial-up
17 Internet access.

18 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

19 **A.** Yes it does.